No. 983

IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1942

Hawkins vs U.S.

E. A. CONWAY, SECRETARY OF STATE,
STATE OF LOUISIANA,

v.

IMPERIAL LIFE INSURANCE CO., IN RECEIVERSHIP, Petitioners,

UNITED STATES OF AMERICA, Opponent and Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE SUPREME COURT OF LOUISIANA.

FRANK J. LOONEY,
Attorney for Petitioner.

ERRATA AND ADDENDA

On page 2, line 1, for "unpublished" read, "reported in Vol. 5, Southern Reporter, 2nd series, No. 3, Jan. 29, 1942, page 314 et seq."

On page 3, line 25, after words "pages 12-13" add "5 Southern Reporter, 2nd, p. 320."

On page 4, line 15, after words "page 13" add "5 Southern Reporter, 2nd, p. 320."

On page 5, line 3, after words "page 19" add "5 Southern Reporter, 2nd, p. 322."

Corrections to conform original transcript references in petition for certiorari with pages of printed record.

Petition

P 3 T58 is R19.

P 3 T59 is R20

P 3 T62 is R22.

P 3 T54 is R16.

P 3 Judgment 12-13 is R122.

P 4 Judgment 13 is R123.

P 4 T155 is R34.

P 4 T156 is R34.

P 4 T167(157) is R36.

P 4 T166-7 is R44.

P 4 T167 is R44.

P 5 T210 is R65-6.

P 5 T212-13 is R67-8.

P 5 Judgment 19 is R126-7.

P 5 T96 is R26.

INDEX.

Citations.

IN THE

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E. A. CONWAY, SECRETARY OF STATE,
STATE OF LOUISIANA,

v.

IMPERIAL LIFE INSURANCE CO., IN RECEIVERSHIP, Petitioners,

UNITED STATES OF AMERICA, Opponent and Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE SUPREME COURT OF LOUISIANA.

Udox N. Hankins, Receiver of the Imperial Life Insurance Company, a Louisiana corporation, domiciled in Shreveport, Caddo Parish, Louisiana, in Receivership, files this petition, and prays that a writ of certiorari issue to review the judgment of the Supreme Court of Louisiana entered in the above case on November 3, 1941.

Opinions Below.

The opinion of the State Supreme Court is unpublished, but appears in photostatic form in the Record.

Jurisdiction.

The judgment of the State Supreme Court became final on refusal of the motion for rehearing on December 1, 1941. The jurisdiction of this Court is invoked under Section 237 of the Judicial Code, as amended February 13, 1925 (U. S. Code T. 28, § 344(b)).

Statute Involved.

The statutes involved are Title 26, Sections 201 and 202, U. S. Code.

Statement.

The Imperial Life Insurance Company, in receivership in the First Judicial District Court of Louisiana, filed a tableau of debts which was opposed by the United States Government, alleging that the company, as transferee of the American Benefit Association, a life insurance company, owed $35,673.53 income taxes for the years 1934 to 1937, inclusive, and as transferee of the Imperial Protective Union, a life insurance company, owed $5974.44 income taxes for the same years; and further claimed $1,364.24 Social Security tax.

The Receiver's defense was that the companies were insurance companies and were liable for income taxes, not on premiums, but only for interest, dividends and rents under the terms of Title 26, Sections 201, 202 and 203 of the United States Code.

The District Judge held that no income taxes were due, finding that:

1st. The companies were mutual life insurance companies (Transcript Supreme Court of Louisiana, p. 58, which transcript is hereafter referred to by the letter "T");

2nd. That the bylaws which governed the contracts between each company and its policy holders required that certain percentages of premiums paid after the first three months be devoted to the Benefit (or Mortuary) Fund, viz., 25% for the next succeeding 12 months; 50% for the second period of 12 months; 60% for the third period of 12 months, which ratio had been strictly adhered to (T. 59);

3rd. That the definition given by Congress in U. S. Code T. 26 § 201 governed, because (a) the business of the companies was life insurance, and (b) that more than 50% of their total reserve was for mortuary and policy benefits (T. 62).

4th. That the Social Security Tax was due by the Imperial Life Insurance Company (T. 54).

A photostatic copy of the Supreme Court's opinion is contained in the record.

The following are excerpts from that Judgment, (pages 12-13):

> "In the sense that they were insuring the lives of their members, the companies were manifestly engaged in the life insurance business. But that is not the question. The question is whether

> they were life insurance companies within the meaning of the term as defined by the federal statute—that is, did these companies keep or accumulate reserve funds to be held for the fulfillment of their insurance contract and, if so, did the reserve funds 'comprise more than 50 per centum of its total reserve funds'? * * * However, there has been no proof submitted by the receiver to demonstrate that this benefit or reserve fund comprised more than 50 per centum of the total reserve funds of the company. In the absence of such proof, the company cannot be properly classified as a life insurance company as defined by Section 201 (a) of the federal statute."

Again, (page 13):

> "The use of the words 'reserve funds' in the definition contained in Section 201 (a) of the statute presupposes, we think, typical legal reserves based on actuarial calculations and recognized tables of mortality or other experience. The Treasury Department has interpreted the provisions of Section 201 (a) in this sense. . (citing regulations)"

There were no disputed facts in the case. The evidence of the Government witnesses, which was the only evidence in the case as to the "reserve fund," was that the fund transferred to the Imperial Life Insurance Company by the American Benefit Association, namely $40,000.00 (T. 155), and that transferred by the Imperial Protective Union, namely $5,085.00 (T. 156), were transferred to the Mortuary Fund of the Imperial Life Insurance Company (T. 167). Also that these transferred funds were from the "Benefit Fund" of the American Benefit Association (T. 166-167) and the "Benefit Fund" of the Imperial Protective Union (T. 167). (Testimony of G. C. Crawford,

Special Agent Intelligence Department, T. 157; also Charlton testimony, T. 210, 212-13). The Louisiana Supreme Court also held (p. 19):

> "The evidence discloses to our satisfaction that the defendant company was a transferee within the meaning of the federal statute and therefore liable for the payment of the income tax due by the transferor companies to the extent of the value of the assets ($45,085) which it received from them. *The defendant, by these transfers, acquired all of the tangible assets of the transferor concerns to the prejudice of the Federal Government and other creditors.*"

The undisputed evidence given by Government witness Charlton (T. 96) is that at the time of the transfers the transferor companies were solvent. There was no other evidence concerning the basis on which the "reserve" was established except that the reserve was based on the contract between the companies and their member certificate holders as required by the by-laws.

Questions Presented.

1. When Congress declares, in U. S. Code T. 26 Section 201(a) that "the term 'life insurance company' means an insurance company engaged in the business of issuing life insurance and annuity contracts (including contracts of combined life, health, and accident insurance) the reserve funds of which held for the fulfillment of such contracts comprise more than 50 per centum of its total reserve funds," has the Supreme Court of Louisiana the right to add to this definition, that this reserve fund must have an "actuarial basis"?

2. When the evidence offered by the Government shows that the "reserve fund" of a life insurance company consists entirely of funds held for the fulfillment of its contracts, as required by U. S. Code Title 26, Section 201(a), is it necessary for a Receiver, whose account filed in a State receivership proceeding is opposed by the United States Government, to offer evidence tending to show that there was no other reserve fund?

Reasons for Granting the Writ.

This case presents a question of general importance in the administration of the Revenue Laws as well as conflict between the decision of the Supreme Court of Louisiana and the Federal Courts.

1. The decision of the Court below is inconsistent with the plain language of the statute, U. S. Code Title 26, Section 201(a), and many federal decisions, and especially, Old Colony R. R. Co. v. Commissioner Internal Revenue, 284 U. S. 552, 561, questioning even the acquaintance of Congress with an "accountant's phrase", and Fox v. Standard Oil Co., 294 U. S. 87, 96, rejecting "substitutes for the definition set before us by the lawmakers."

2. The decision of the Court below violates a precept of law generally acknowledged and especially declared in New Orleans Railway Company v. National Rice Mill Co., 224 U. S. 80, holding, "The plaintiff was entitled to the benefit of all the testimony in the case from whatever source it came . . . even though having the burden of proof"; and numerous decisions holding that the presumption in favor of a Commissioner's finding is only *prima facie* and the Board of Tax Appeals has no right to reject

even expert testimony overturning same without personal knowledge. See Belridge Oil Co. v. Comm. Internal Revenue, 85 F. (2d) 762, 763.

3. The decision below misconstrues the decisions of the United States Supreme Court in all cases cited on Treasury Regulation 86, Revenue Act of 1934, which held that the Treasury regulation applied to deductions—but they did not pretend to affect or change the definitions in the revenue laws.

CONCLUSION.

For the foregoing reasons, it is respectfully submitted that this petition should be granted.

FRANK J. LOONEY,
Attorney for Petitioner.

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CITATIONS

454382—42

In the Supreme Court of the United States

OCTOBER TERM, 1941

No. 983

UDOX N. HANKINS, RECEIVER OF THE IMPERIAL LIFE INSURANCE COMPANY, PETITIONER

v.

THE UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE SUPREME COURT OF THE STATE OF LOUISIANA

BRIEF FOR THE UNITED STATES IN OPPOSITION

OPINIONS BELOW

The opinion of the District Court for the First Judicial District for the Parish of Caddo (R. 15–24) is not reported. The opinion of the Supreme Court of Louisiana (R. 114–128) is reported in 5 So. (2d) 314.

JURISDICTION

The judgment of the Supreme Court of Louisiana was filed November 3, 1941 (R. 114). A petition for rehearing was denied December 1, 1941 (R. 134). The petition for a writ of certiorari was filed February 27, 1942. The jurisdiction of this Court

is invoked under Section 237 (b) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Should two companies issuing contracts calling for death benefits but maintaining no reserves of an actuarial nature be classified for tax purposes as life insurance companies under Section 201 (a) of the Federal Revenue Acts of 1934 and 1936?

STATUTES AND REGULATIONS INVOLVED

The statutes and regulations involved are set forth in the Appendix, *infra,* pp. 8–12.

STATEMENT

The pertinent facts, which are not in dispute, are as follows:

In 1938 a receivership proceeding was instituted against the Imperial Life Insurance Company, a Louisiana company, in the First Judicial District Court for the Parish of Caddo. Petitioner was appointed receiver and filed a tableau of the Company's debts. The United States opposed the tableau on the ground that the Company was indebted to it for unpaid social security and income taxes for the years 1934 through 1937. The income taxes amounting to $41,647.97 originally had been assessed against the American Benefit Association and the Imperial Protective Union. These companies, which were organized under the laws of Colorado and Delaware, respectively, but

did business only in Louisiana, had transferred their assets to the Imperial Life Insurance Company in 1937. (R. 15–17, 114–117.)

The income taxes were assessed against the transferor companies under the provisions applicable to regular corporations. The receiver contended, however, that the companies were life insurance companies as defined in Section 201 (a) of the Revenue Acts of 1934 and 1936. (Appendix, *infra,* p. 8.) It was conceded that if they were such companies, no taxes were due. The evidence showed that during the tax years each company issued contracts calling for the payment of sums of money on the death or disability of the persons who were covered by the contracts. But neither company maintained reserves computed on an actuarial basis from mortality or other tables of experience (R. 23, 122–123). Moreover, the certificate of incorporation of the American Benefit Association stated that it was not to be deemed an insurance company (R. 104), and that of the Imperial Protective Union contained a similar provision (R. 16).

The District Court sustained the claim of the United States for the social security taxes but overruled its claim for the income taxes. It held that Section 201 (a) did not require the maintenance of reserves of an actuarial nature, and that the Commissioner had erred in not classifying the companies as insurance companies (R. 15–24).

On appeal by both parties the Supreme Court of Louisiana affirmed the ruling with respect to the social security taxes, and the petition raises no question as to them. The Supreme Court reversed the decision of the District Court with respect to the income taxes. It held that the companies were not life insurance companies as defined in Section 201 (a), because (1) petitioner had not proved that the Imperial Protective Union maintained any reserve fund for the payment of claims on its contracts or that the American Benefit Association maintained such a reserve in excess of 50% of its total reserves; and (2) because, in any event, neither company maintained reserves based on actuarial calculations. (R. 122–128.)

ARGUMENT

Since petitioner contends that the transferor companies were entitled to the exceptional tax treatment accorded life insurance companies as defined in Section 201 (a), it was incumbent upon him to show by clear evidence that the statutory requirements were met. *Bowers* v. *Lawyers Mortgage Co.*, 285 U. S. 182, 187. This, however, was not done.

Section 201 (a) provides that:

> When used in this title the term "life insurance company" means an insurance company engaged in the business of issuing life insurance and annuity contracts (including contracts of combined life, health,

> and accident insurance), the reserve funds of which held for the fulfillment of such contracts comprise more than 50 per centum of its total reserve funds.

Evidence was introduced that both companies maintained small "Benefit Fund" accounts as their only alleged reserves (R. 41–44, 63–66, 78). But the record is not clear as to whether more than 50% of the benefit funds were held for the fulfillment of contracts fitting the statutory description (See R. 41, 65, 78, 118). Moreover, there is no evidence whatever and it is not contended that the benefit funds or any other reserves were maintained on an actuarial basis. This circumstance is alone sufficient to support the decision.

While Congress did not in terms specify that the words "reserve funds" as used in Section 201 (a) mean reserve funds based on some recognized table of mortality experience, there seems little doubt that it intended them to be so construed. See *Helvering* v. *Inter-Mountain Life Insurance Co.*, 294 U. S. 686, 690; *Helvering* v. *Illinois Ins. Co.*, 299 U. S. 88, 91. The reserve funds typically maintained by and required of life insurance companies are of that character and it is not to be supposed that in defining "life insurance company" for purposes of exemption from taxation as regular corporations Congress would have meant to include any company not having such reserves. Cf. *Helvering* v. *Oregon Ins. Co.*, 311 U. S. 267, 268–270.

Treasury Regulations 86 and 94 (Appendix, *infra*, pp. 10–12), promulgated under the Revenue Acts of 1934 and 1936, respectively, define the "reserve" contemplated by Section 201 (a) as being, in general, a sum "variously computed or estimated, which, with accretions from interest, is set aside (reserved) as a fund with which to mature or liquidate * * * future unaccrued and contingent claims." Taken alone this language might be interpreted to cover reserves even though not computed on an actuarial basis. However, the regulations provide further that the reserve "must be required either by express statutory provisions or by rules and regulations of the insurance department of a State". Such a legal reserve, so far as we are aware, would always be calculated from tables of mortality or other experience.

Petitioner asserts (Pet. 6) that the decision of the court below is inconsistent with *Old Colony R. Co.* v. *Commissioner*, 284 U. S. 552; *Fox* v. *Standard Oil Co.*, 294 U. S. 87; and *New Orleans & N. E. R. R. Co.* v. *National Rice Co.*, 234 U. S. 80. But none of those cases dealt with the statutory provisions here involved or is otherwise pertinent to the question of the meaning of the words "life insurance company" or "reserve."

CONCLUSION

The decision of the court below is correct and there is no conflict. The petition therefore should be denied.

Respectfully submitted,

CHARLES FAHY,
Solicitor General.
SAMUEL O. CLARK, Jr.,
Assistant Attorney General.
SEWALL KEY,
GERALD L, WALLACE,
MICHAEL H. CARDOZO, IV.,
Special Assistants to the Attorney General.

APRIL, 1942.

APPENDIX

Revenue Act of 1934, c. 277, 48 Stat. 680:

SEC. 201. TAX ON LIFE INSURANCE COMPANIES.

(a) *Definition.*—When used in this title the term "life insurance company" means an insurance company engaged in the business of issuing life insurance and annuity contracts (including contracts of combined life, health, and accident insurance), the reserve funds of which held for the fulfillment of such contracts comprise more than 50 per centum of its total reserve funds.

(b) *Rate of Tax.*—In lieu of the tax imposed by section 13, there shall be levied, collected, and paid for each taxable year upon the net income of every life insurance company a tax as follows:

(1) In the case of a domestic life insurance company, 13¾ per centum of the amount of its net income in excess of the credit provided in subsection (c) of this section;

* * * * *

(U. S. C., Title 26, Sec. 201.)

SEC. 202. GROSS INCOME OF LIFE INSURANCE COMPANIES.

(a) In the case of a life insurance company the term "gross income" means the gross amount of income received during the taxable year from interest, dividends, and rents.

(b) The term "reserve funds required by law" includes, in the case of assessment insurance, sums actually deposited by any company or association with State or Terri-

torial officers pursuant to law as guaranty or reserve funds, and any funds maintained under the charter or articles of incorporation of the company or association exclusively for the payment of claims arising under certificates of membership or policies issued upon the assessment plan and not subject to any other use. (U. S. C., Title 26, Sec. 202.)

SEC. 203. NET INCOME OF LIFE INSURANCE COMPANIES.

(a) *General Rule.*—In the case of a life insurance company the term "net income" means the gross income less—

(1) *Tax-free interest.*—The amount of interest received during the taxable year which under section 22 (b) (4) is excluded from gross income;

(2) *Reserve funds.*—An amount equal to 4 per centum of the mean of the reserve funds required by law and held at the beginning and end of the taxable year, except that in the case of any such reserve fund which is computed at a lower interest assumption rate, the rate of 3¾ per centum shall be substituted for 4 per centum. Life insurance companies issuing policies covering life, health, and accident insurance combined in one policy issued on the weekly premium payment plan, continuing for life and not subject to cancelation, shall be allowed, in addition to the above, a deduction of 3¾ per centum of the mean of such reserve funds (not required by law) held at the beginning and end of the taxable year, as the Commissioner finds to be necessary for the protection of the holders of such policies only;

* * * * *

(U. S. C., Title 26, Sec. 203.)

The corresponding provisions of the Revenue Act of 1936, c. 690, 49 Stat. 1668, are identical with the foregoing, with exceptions immaterial herein.

Treasury Regulations 86, promulgated under the Revenue Act of 1934:

> ART. 201 (a)-1. *Life insurance companies: Definition.*—The term "life insurance company" as used in Title I is defined in section 201 (a). In determining whether an insurance company is a "life insurance company" as defined in section 201 (a), no reserve shall be regarded as held for the fulfillment of an insurance contract unless it conforms to the definition of "reserve" contained in article 203 (a) (2)-1.
>
> * * * * *
>
> ART. 203 (a) (2)-1. *Reserve funds.*—In general, the reserve contemplated is a sum of money, variously computed or estimated, which, with accretions from interest, is set aside (reserved) as a fund with which to mature or liquidate, either by payment or reinsurance with other companies, future unaccrued and contingent claims. It must be required either by express statutory provisions or by rules and regulations of the insurance department of a State, Territory, or the District of Columbia when promulgated in the exercise of a power conferred by statute, but such requirement, without more, is not conclusive; for example, it does not include reserves required to be maintained to provide for the ordinary running expenses of a business definite in amount, and which must be currently paid by every company from its income if its business is to continue, such as taxes, salaries, reinsurance and unpaid brokerage; the reserve or net value of risks reinsured in other solvent

companies to the extent of the reinsurance; reserve for premiums paid in advance; annual and deferred dividends; accrued but unsettled policy claims; losses incurred but unreported; liability on supplementary contracts not involving life contingencies; estimated value of future premiums which have been waived on policies after proof of total and permanent disability.

In any case where reserves are claimed, sufficient information must be filed with the return to enable the Commissioner to determine the validity of the claim. Reference should be made to the item in which the reserve appears in the annual statement and to the statute or insurance department ruling requiring that such reserves be held. Only reserves which are so required, which are peculiar to insurance companies, and which are dependent upon interest earnings for their maintenance will be considered. A company is permitted to make use of the highest aggregate reserve called for by any State or Territory or the District of Columbia in which it transacts business, but the reserve must have been actually held.

In the case of life insurance companies issuing policies covering life, health, and accident insurance combined in one policy issued on the weekly premium payment plan, continuing for life and not subject to cancellation, it is required that reserve funds thereon be based upon recognized tables of experience covering disability benefits of the kind contained in policies issued by this particular class of companies. The deduction in respect of such reserve funds (not required by law) is 3¾ per cent of the mean of such reserve funds held at the beginning and end of the taxable year.

The corresponding provisions of Treasury Regulations 94, promulgated under the Revenue Act of 1936, are identical with the foregoing, with exceptions immaterial herein.

U. S. GOVERNMENT PRINTING OFFICE: 1943